

STRENGTHENING THE FARM SAFETY NET

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Mr. Chairman and Members of the Subcommittee, thank you for this opportunity to discuss our proposal to strengthen the Federal farm safety net and the crop insurance program. I commend you for starting this critical discussion early in the legislative year.

Last year, a combination of falling crop prices, regional weather disasters, and the impact of multiple-year losses stretched our Federal support programs to the limit. Families who have been in farming for generations found themselves with deeper financial challenges effecting their ability to stay on the farm.

As a result, Congress and the Administration agreed on the need for government to intervene and provide help through a \$6 billion emergency farm aid package. At the same time, President Clinton and Secretary Glickman began a process of examining options for more permanent improvements to our government programs aimed at helping farmers cope with volatile conditions.

The current crop insurance program was designed to work in conjunction with agricultural programs that no longer exist. Once those programs were eliminated, it was apparent that the current crop insurance program was inadequate to fill the void on its own.

Reform is needed if farmers are to have the tools they need to successfully manage their agricultural risks. In his State of the Union message, President Clinton pledged to work with Members of Congress of both parties to create a farm safety net that includes an improved federal crop insurance program.

Earlier this month, USDA presented specific ideas for strengthening the farm safety net with the announcement of the FY2000 budget. Since then, we have further refined our ideas and want to work with Congress to invest additional funds to enhance the crop insurance program for farmers. Before outlining our specific plans to improve the program, I would like to review some of the factors that have brought us to this critical juncture in agricultural policy.

Background

Prior to 1994, crop insurance ran side-by-side with ad hoc disaster assistance. Under ad hoc disaster programs, farmers were in a constant state of uncertainty over whether, how much, and when disaster assistance might be provided. Further, disaster programs were prone to abuse, and created an unmanageable drain on tax dollars. The availability of free disaster assistance also undercut participation in the crop insurance program and as a result, the crop insurance program never achieved sufficient participation to become the primary source of federal assistance for farmers suffering a crop loss.

In 1994, the Administration proposed legislative reforms to replace ad hoc disaster assistance in favor of an enhanced crop insurance program. Under that plan, farmers could obtain catastrophic risk protection (CAT) level of insurance for a nominal administrative fee. In addition, premium subsidies were increased for producers choosing to obtain higher levels of coverage. The legislation also created a non-insured crop disaster assistance program (NAP) for crops that are not currently insurable.

In its proposals to Congress for the 1996 Farm Bill, the Administration recommended and Congress approved enhancing crop insurance by authorizing USDA to offer revenue insurance. Congress also directed USDA to help farmers become better risk managers, eliminated both the requirement that producers obtain crop insurance to participate in most USDA farm programs and began the phase-out of direct-subsidy programs which had been the heart of traditional farm policy. The result of these changes is that farmers have been placed on a steep learning curve to learn new ways of doing business at a time they also face unprecedented challenges in the form of low prices.

In 1998, commodity prices plummeted while many farmers struggled to cope with the effects of natural disasters, sometimes spanning several years. In short, the concerns raised by passage of the 1996 Farm Bill became reality. Neither crop insurance nor the other 1996 Farm Bill programs were able to provide the amount of assistance required—resulting in a \$6 billion emergency relief package.

Although the current crop insurance program must be enhanced to respond adequately to current conditions, it has made significant progress. For example, in 1993, the program provided \$11.3 billion in protection through 70,000 policies on 83.7 million acres of crops. In 1998, crop insurance provided \$27.9 billion in protection through 1.2 million policies on 181.6 million acres.

This increase in participation was partly due to the significant increase in the number and types of insurance plans available. For example, prior to 1996, no federally backed revenue insurance products were available to producers. Today, there are five different types of revenue insurance available: Income Protection (IP), Revenue Assurance (RA), Crop Revenue Coverage (CRC), Gross Revenue Income Protection (GRIP), and Adjusted Gross Revenue (AGR). Revenue insurance protects farmers against price declines, not just production losses from natural disasters.

Because crop insurance helps producers manage their risk and diversify their operations, there has been an aggressive effort to create new programs and expand the availability of existing ones. In 1998 alone, pilot programs were developed for avocados, sweet cherries, rangeland, winter squash, mustard, crambe, cabbage, watermelon, and wild rice.

Consistent with its commitment to building a stronger crop insurance program, USDA supported a provision included in the FY1999 Omnibus Reconciliation Bill, requiring uninsured recipients of the emergency assistance to obtain insurance over the next 2 years. More significantly, to encourage greater participation in crop insurance and as a down payment on crop insurance reform, USDA earmarked \$400 million from the emergency aid program to provide most farmers a one-time, 30-percent reduction of their crop insurance premiums.

Concerns

In 1998, emergency aid was provided and a financial crisis of enormous proportions was deferred. However, in future years, the new system needs to work without ad hoc infusions of tax dollars.

To preclude a repeat of 1998, the following weaknesses must be addressed this year:

- ❖ Basic CAT coverage in most cases has not been sufficient to provide farmers an adequate safety net in times of severe stress, and not enough farmers buy higher levels of coverage—only two-thirds of the farmers who have crop insurance purchase buy-up coverage.
- ❖ Farmers generally obtain insurance based on expected market prices established at the start of the year, which may vary significantly from actual prices at the time of harvest. Also, current insurance products do not protect them against low prices that carry over annually.
- ❖ Farmers who experience several years of adverse weather may be unable to obtain enough insurance to cover their costs of production because the amount of coverage they can buy is linked to, and limited by, their actual production history. In many cases, farmers find their insurable yields declining as their premium rates increase—a problem especially acute in the Great Plains.
- ❖ While growing, participation in revenue insurance, which protects against falling prices, remains relatively limited. Only about 16 percent of the corn and soybean farmers who purchase higher levels of coverage take revenue insurance.
- ❖ Measured in value of sales, the livestock industry represents the biggest segment of American agriculture; however, the current law does not permit USDA to extend coverage for livestock losses. The private sector only insures against livestock mortality, and this coverage is only used sparingly.
- ❖ Crop insurance programs have not yet been developed for many important and economically significant crops. Thus, these producers are protected only through the limited coverage offered by NAP.
- ❖ Crop insurance is governed by contractual and regulatory restrictions that often make it unable to respond quickly and flexibly to changing needs of the farmer, unanticipated events, or unforeseen program flaws. The program is least effective in those areas of the country where participation is low, certain crops are uninsurable, or where multiple years of disaster have occurred.

Guidelines for Reform

USDA believes that any legislation to strengthen the farm safety net should address the following principles:

- ❖ **Maximize participation**—Farm programs as well as crop insurance should assist as many farmers and ranchers as possible by making the (insurance) program more affordable. Re-establishing linkage with other USDA programs should be considered.
- ❖ **Provide comprehensive coverage**—Insurance coverage should be as comprehensive as possible, covering as many commodities (including livestock) and risks as possible.
- ❖ **Use market mechanisms**—Both farm programs and crop insurance should fully use market mechanisms.
- ❖ **Increase flexibility**—The crop insurance program should be flexible enough to meet the diverse demands posed by the varied risks farmers and ranchers face.
- ❖ **Provide programs at the lowest cost to taxpayers**—These programs should be delivered at the lowest possible cost to both taxpayers and farmers and ranchers.

Proposals for Change

As indicated earlier in my testimony, USDA has been refining the initial proposal to strengthen the crop insurance program:

- ❖ **Raise the coverage floor**—In 1998, nearly 32 percent of crop insurance policies were at the CAT level of coverage. Since CAT and NAP levels of coverage protect less than a third of the crop value, crop insurance reform legislation should increase the coverage available under these programs. Specifically, we propose to raise the coverage to 60 percent of approved yield indemnified at 70 percent of the expected market price, a 50 percent increase. Caution is needed to avoid raising buy-up insurance too high thereby shifting production and potentially depressing prices further. Caution is also needed to avoid raising CAT coverage too high due to the potential buy-down affect on current buy-up policy holders.
- ❖ **Make higher-level coverage more affordable**—Crop insurance reform should increase incentives for farmers to buy more comprehensive insurance at higher buy-up levels. Specifically, we propose to (a) increase the premium subsidy so that coverage at 70 percent of the approved yield indemnified at 100 percent of the expected market price level (or 70/100) will cost the producer the same as 65/100 coverage does today; (b) provide an additional premium subsidy for coverage above the 70/100 level of 50 percent of the additional premium; and make all insurance plans, including revenue, equal in terms of assistance for premiums; review of company expense reimbursements may be warranted in recognition of the higher premium. The subsidy rate at these higher coverage levels would be 55%.

❖ **Cover multi-year disasters**—To address the special concerns raised by multi-year crop losses and losses not severe enough to trigger current loss requirements, crop insurance reform should authorize USDA to offer a new multi-year insurance product. Specifically, we propose to develop a new multi-year insurance "umbrella" to complement single-year policies. Further, crop insurance price elections and company expense payments would be based on multi-year price averages, avoiding sharp inter-year swings. In this context, RMA would also examine alternatives to the current method of determining the yields used as the basis for coverage.

❖ **Speed flexible, new risk management tools to market**—To meet the changing needs of farmers and ranchers, crop insurance reform should provide farmers more flexible products to cover their diverse needs, including more types of revenue-based insurance products. Crop insurance reform should permit USDA to work more creatively with private insurance companies and others to develop and bring to market new risk management tools and give USDA more flexibility to use and expand pilot projects. Specifically, we propose to stimulate the flow of new risk management tools to farmers by: (a) authorizing the Risk Management Agency to reimburse companies for costs of successful new products that they develop; (b) expanding contracting with the private sector to develop products for smaller crops; (c) reducing the regulatory procedures required to develop and update policies; and (d) giving RMA greater flexibility to use pilot projects, including pilot programs on a nationwide scale.

❖ **Cover livestock**—Because the current crop insurance program does not cover livestock producers, who make up the largest single sector of American agriculture in terms of value of production, crop insurance reform should include provisions to enable USDA to cover livestock. Specifically, USDA proposes authorizing RMA to pilot revenue-based livestock insurance products proposed by the private sector. On an initial basis, we propose providing up to \$50 million per year from the FCIC fund for these products.

❖ **Improve the NAP program**—Many farmers rely on the NAP program as their primary protection from natural disaster losses. Coverage should be increased to 60% of yield and 70% of price, commensurate with the CAT increase. In addition, the cost-effectiveness of the current area trigger versus a Secretarial disaster designation should be reviewed.

❖ **Provide better information and service to farmers**— As we make these changes to strengthen the crop insurance program as part of the farm safety net, it will also be important that we increase farmer awareness so that producers can more quickly access a wide range of both new and existing risk management tools. Crop insurance reform should include a public awareness outreach effort to enable producers to assume more responsibility for greater understanding, and to better manage their risk management planning portfolios, backed by an annual financial commitment of up to \$50 million.

Taken together, these proposals would constitute a major financial investment by the Federal government that would total between \$2 and \$2.5 billion per year. The Administration is ready to work with you to refine these proposals so we can agree on a mutually acceptable reform package and to identify the amount and sources of funds these changes will require.

While the crop insurance program is the anchor of the farm safety net, USDA also wants to work with Congress to examine other programs to assist farmers and ranchers.

The Next Step

Recently, Secretary Glickman wrote:

Farmers deserve better than to be a political football for Democrats and Republicans to toss around. So, whatever approach we adopt, we have to do it in a bipartisan fashion. It just makes sense that the more people you have contributing to the process, the better the ideas that emerge.

In that spirit, USDA began to formulate the basics of a workable plan last August when the Secretary convened a group of farmers and other experts from all sectors of the agricultural community. The results of that effort were refined and have become the basis of our proposal. To help new ideas surface and build consensus on these elements of reform, Secretary Glickman, Deputy Secretary Rominger, and Under Secretary Schumacher plan to host a series of forums over the next several months to hear from everyone who has a stake in building or benefitting from a strong and enduring farm safety net.

Mr. Chairman, there is no question that many decisions must be made to provide producers the safety net they deserve. I am confident that the good will and common sense needed to make this vision a reality will prevail. Thank you for this opportunity to participate in this hearing.